

Message Text

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ACTION EB-07

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FRB-01 INR-07 NSAE-00 USIA-15 TRSE-00 XMB-04 OPIC-06

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SUBJECT: EXCHANGE CONTROL AMNESTY; "FRANCO VALUTA" IMPORTS;
DOLLAR INDEXED LOAN

PASS TREASURY AND FRB

REF: ROME A-325 (NOTAL)

/SUMMARY/. ON AUGUST 10 ITALIAN CABINET APPROVED DECREE
LAW TO EXTEND PERIOD OF EXCHANGE CONTROL AMNESTY (REPORTED
REFAIR) BY 90 DAYS. RELATED PROPOSALS WHICH WOULD CREATE
SYSTEM OF "FRANCO VALUTA" IMPORTS (IMPORTS WITHOUT NEED FOR
FOREIGN EXCHANGE PAYMENTS) AND WHICH WOULD AUTHORIZE SPECIAL
DOLLAR INDEXED BOND ISSUE HAVE BOTH BEEN SET ASIDE PENDING
PARLIAMENTARY DISCUSSION OF THESE MATTERS IN SEPTEMBER.
/END SUMMARY/.

1. /EXCHANGE CONTROL AMNESTY/. DECREE LAW JUST APPROVED BY
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CABINET WILL EXTEND UNTIL NOVEMBER 19 DEADLINE FOR DECLARING

TO EXCHANGE CONTROL AUTHORITIES ILLEGALLY HELD FOREIGN CURRENCY ASSETS WHICH ITALIAN RESIDENTS WISH TO REPATRIATE UNDER EXCHANGE CONTROL AND TAX AMNESTY PROVISIONS OF LAW NO. 159 OF APRIL 30, 1976 (WHICH CONVERTED INTO LAW AND MODIFIED DECREE LAW NO. 31 OF MARCH 4, 1976). SIMILARLY DEADLINE FOR ACTUAL REPATRIATION OF LIQUID ASSETS HAS BEEN EXTENDED UNTIL FEBRUARY 19, 1977. NO OTHER CHANGES WERE MADE IN LAW 159. NEW DECREE LAW MUST NOW BE RATIFIED BY PARLIAMENT, WHICH IS EXPECTED TO CONSIDER MATTER IN SEPTEMBER.

2. /"FRANCO VALUTA" IMPORTS/. PROPOSAL FOR RE-INTRODUCING "FRANCO VALUTA" IMPORT SYSTEM HAS AT LEAST TEMPORARILY BEEN SHELVED. DRAFT PROPOSAL WOULD HAVE ENCOURAGED PAYMENT FOR IMPORTS WITH ILLEGALLY-EXPORTED CAPITAL BY PERMITTING ITALIAN IMPORTERS TO IMPORT GOODS "FRANCO VALUTA", I.E., WITHOUT HAVING TO PURCHASE FOREIGN EXCHANGE IN ITALY. IN TURN, ITALIAN EXCHANGE CONTROL AND TAX AUTHORITIES WOULD ASK NO QUESTIONS ABOUT FOREIGN SOURCE OF PAYMENT FOR SUCH IMPORTS. SINCE THERE WOULD BE NO NEED TO PURCHASE FOREIGN EXCHANGE, IMPORTS WOULD BE EXEMPT FROM CURRENT PRIOR DEPOSIT REQUIREMENT. REPORTEDLY, ALL TYPES OF IMPORTS WOULD BE COVERED BY SYSTEM, SINCE SELECTIVE APPROACH MIGHT RAISE PROBLEMS WITH ITALY'S TRADING PARTNERS, ESPECIALLY EC. APPARENTLY PROPOSED SYSTEM WOULD BE INTRODUCED ON TEMPORARY BASIS, TO TERMINATE ON SAME DATE AS FOREIGN EXCHANGE CONTROL AMNESTY (I.E., NOVEMBER 19, 1976).

3. /DOLLAR INDEXED LOAN/. IN ADDITION TO "FRANCO VALUTA" IDEA, POSSIBLE DOLLAR INDEXED LOAN WAS ALSO CONTAINED IN ANDREOTTI GOVERNMENT ECONOMIC PROGRAM. REPORTEDLY, POSSIBLE LOAN WOULD HAVE FOLLOWING CHARACTERISTICS: (1) DOLLAR DENOMINATED, (2) SUBSCRIBABLE IN VARIOUS CONVERTIBLE FOREIGN CURRENCIES DURING PERIOD ENDING NOVEMBER 19, 1976, (3) REDEEMABLE IN NON-CONVERTIBLE LIRE, (4) NEGOTIABLE IN FORM OF BEARER BONDS, (5) INTEREST-BEARING AT PREVAILING EUROMARKET RATES, (6) MATURING IN FIVE YEARS, AND (7) OPEN-ENDED AS TO AMOUNT. PRESS ORIGINALLY SPECULATED THAT BONDS MIGHT ATTRACT \$2-3 BILLION IN ITALIAN CAPITAL HELD ABROAD. HOWEVER, FOREIGN TRADE MINISTRY SOURCES REPORTEDLY ANTICIPATE THAT BOND ISSUE WOULD UNCLASSIFIED

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NOT ATTRACT MORE THAN ABOUT \$100-200 MILLION.

4. /COMMENT/. ABOVE THREE MEASURES, WHICH ARE ALL DESIGNED TO ENCOURAGE REPATRIATION OF ILLEGALLY-EXPORTED CAPITAL, HAVE GIVEN RISE TO LIVELY DEBATE ON QUESTION OF WHETHER BALANCE OF PAYMENTS NEEDS ARE SUFFICIENTLY IMPORTANT TO OVERRIDE CONCERN ABOUT "REWARDING" PAST ILLEGAL BEHAVIOR. WHILE ITALY'S DIFFICULT BALANCE OF PAYMENTS SITUATION IS WIDELY

APPRECIATED AND THERE IS GENERAL SUPPORT FOR EFFORTS TO ENCOURAGE CAPITAL REFLOWS, POLITICAL PARTIES, ESPECIALLY COMMUNISTS (PCI) AND SOCIALISTS (PSI) ARE EMBARRASSED TO BE SUPPORTING MEASURE WHICH SEEMS TO FAVOR ILLEGAL CAPITAL EXPORTERS AS AGAINST LAW-ABIDING CITIZENS. ORIGINAL INTENT OF LAW 159 WAS, IN FACT, TO PUNISH CAPITAL EXPORTERS AND OTHER VIOLATORS OF EXCHANGE CONTROL REGULATIONS BY INTRODUCTION OF CRIMINAL PENALTIES FOR EXCHANGE CONTROL VIOLATIONS INSTEAD OF ONLY IMPOSING FINES. AMNESTY PROVISION WAS MERELY DESIGNED TO PERMIT TEMPORARY SUSPENSION OF APPLICATION OF THESE NEW PENALTIES. WHILE NO FIGURES HAVE BEEN GIVEN AS TO AMOUNTS OF FOREIGN CURRENCY WHICH HAVE BEEN DECLARED UNDER AMNESTY PROVISION, MINISTER OF FOREIGN TRADE OSSOLA TOLD PRESS THAT NO MORE THAN 100 STATEMENTS HAVE BEEN FILED AND AMOUNTS ARE BELIEVED TO BE SMALL.

5. AT FIRST, PRESS REPORTS ON AUGUST 11 INDICATED THAT GOI WAS ABOUT TO INTRODUCE BOTH "FRANCO VALUTA" AND DOLLAR INDEXED LOAN PROPOSALS. HOWEVER, WIDESPREAD CRITICISM OF THESE MEASURES HAS NOW CAUSED GOVERNMENT TO SET ASIDE BOTH PROPOSALS UNTIL IT HAS HEARD OPINION OF PARLIAMENT, PRESUMABLY DURING SEPTEMBER DEBATE ON RATIFICATION OF 90-DAY EXTENSION OF AMNESTY. CRITICISM MAINLY CONSISTS OF OPPOSITION TO "REWARDING" ILLEGAL CAPITAL EXPORTERS. HOWEVER, CRITICS HAVE ALSO POINTED OUT SOME TECHNICAL PROBLEMS REGARDING POSSIBLE DOLLAR-DENOMINATED LOAN ISSUE. FIRST IS DANGER OF TRIGGERING CIRCULAR FLOW OF CAPITAL, WHEREBY ITALIAN RESIDENTS WOULD ILLEGALLY EXPORT CAPITAL IN ORDER TO IMMEDIATELY REPATRIATE IT TO PURCHASE SUCH BONDS. RESULT WOULD BE NO BALANCE OF PAYMENTS GAIN. SECOND IS DANGER THAT COMPETITION FROM THIS TYPE OF BOND COULD DEPRESS DOMESTIC BOND PRICES.

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6. EVIDENCE SUGGESTS THAT THERE HAS BEEN SOME CAPITAL INFLOW SINCE JUNE 20 ELECTIONS. IT IS DOUBTFUL, HOWEVER, THAT EXCHANGE CONTROL AMNESTY HAS BEEN A VERY IMPORTANT FACTOR. MORE LIKELY SOME REFLOWS CAN BE ATTRIBUTED TO REPATRIATION OF CAPITAL EXPORTED DURING ELECTION PERIOD IN FEAR OF DIRECT COMMUNIST ENTRY INTO GOVERNMENT. OTHER IMPORTANT FACTORS ARE CONTINUED HIGH INTEREST RATES IN ITALY DURING PERIOD OF ECONOMIC RECOVERY. THIS HAS NO DOUBT ENCOURAGED SMALL AND MEDIUM BUSINESSES TO REPATRIATE CAPITAL HELD ABROAD IN ORDER TO FINANCE WORKING CAPITAL AND INVESTMENT NEEDS WITHOUT HAVING TO RESORT TO DOMESTIC BANK CREDIT WHERE OFFICIAL PRIME RATE IS NOW 19.5 PERCENT. VOLPE

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